Alberta

2013-14 **Third Quarter** Fiscal Update and Economic Statement

The **Building Alberta** Plan

February 2014

Table of Contents

ACTUAL RESULTS 3

- Operational Plan Highlights 4
- Operational Plan Summary 4
- Revenue 5
- Operating Expense by Ministry 6
- Disaster / Emergency Assistance 6
- Capital Amortization 7
- Inventory Consumption 7
- Debt Servicing Costs 8
- 2013-14 Financing Requirements 8
- Inventory Acquisition 8
- Capital Plan Highlights 9
- Capital Plan Summary 9
- Capital Plan by Ministry 9

ECONOMIC OUTLOOK

- Alberta economy enters 2014 firing on all cylinders 10

KEY ENERGY AND ECONOMIC ASSUMPTIONS 12

THE CANADIAN DOLLAR

- What does a weaker loonie mean for Alberta? 13

REVENUE IMPACTS

- Impacts of recent developments on government revenue 15

***NOTE:** Amounts presented in tables may not add to totals due to rounding.*

Alberta

ADDITIONAL COPIES OF THIS REPORT

may be obtained by visiting our website at: www.finance.alberta.ca/publications/budget/index.html

ACTUAL RESULTS

For the first nine months of 2013–14

Method of Consolidation

The *2013-14 Third Quarter Fiscal Update and Economic Statement* reports on the same scope, using the same method of consolidation, as presented in *Budget 2013*.

The results of all government departments, funds and agencies, except those designated as government business enterprises, are consolidated on a line-by-line basis. Revenue and expense transactions between consolidated entities have been eliminated.

The accounts of provincial agencies designated as government business enterprises are included on the modified equity basis, the equity being computed in accordance with International Financial Reporting Standards applicable to those entities.

The accounts of the Alberta Innovates corporations and the Crown-controlled SUCH sector organizations such as school boards, universities, colleges, technical institutes, and Alberta Health Services that are controlled by the government are not included in this fiscal summary. These Crown-controlled entities are consolidated on a line-by-line basis in the consolidated financial statements forming part of the *Government of Alberta Annual Report*.

Basis of Financial Reporting

The consolidated fiscal summary reports revenue (including gains from disposal of tangible capital assets), expense (including amortization, loss on disposal and write-down of tangible capital assets), and surplus / (deficit).

Revenue and expense are recorded using the accrual basis of accounting. Cash received for goods or services which have not been provided by period end is recorded as unearned revenue.

Transfers received for capital purposes, and donated capital assets, are recorded as revenue as the cash is used to acquire capital assets and the donated assets are added to the balance sheet. The accounting policy followed in the Consolidated Financial Statements is to record a "deferred capital contribution," similar to a liability, when the cash or asset is received, and to recognize the revenue over the related asset's useful life (in effect matching the asset's amortization expense).

Expense includes the province's cash payments towards the unfunded pension liabilities. Expense excludes the change in the unfunded pension liabilities, which is a non-cash expense that does not affect borrowing requirements.

Debt servicing costs include interest payable, and amortization of issue costs and discounts / premiums on debt issues.

Compliance with Legislation

The *Fiscal Management Act* requires reporting on the fiscal plan actual results for the first nine months of the fiscal year (April 1 to December 31), on or before February 28. The Act gives the President of Treasury Board and Minister of Finance discretion over the form of the report.

The *2013-14 Third Quarter Fiscal Update and Economic Statement* provides comparisons between the nine month estimates and actual results for: revenue and operational expense; the operational surplus / (deficit); the Capital Plan; financing (borrowing) requirements. Also included are an estimate for the year-end balance of the Contingency Account, to indicate the Province's net financial position, and an updated Alberta economic outlook, with associated assumptions.

Under the *Fiscal Management Act*, operating expense increases, excluding those for dedicated revenue-operating expense, collective bargaining or other remuneration settlements, or settlements with First Nations, are limited to 1% of total budgeted ministry operating expense. Actual operational expense for a fiscal year also cannot exceed operational revenue plus any amounts allocated from the Contingency Account.

This report, and results for the first nine months of 2013-14, are in compliance with the requirements of the *Fiscal Management Act*.

2013-14 THIRD QUARTER FISCAL UPDATE

Operational Plan Highlights

Actual results for the first nine months of 2013-14 produced an operational surplus of $1.2 billion, $1.6 billion higher than the *Budget 2013* estimate, due to a $2.7 billion increase in operational revenue, partially offset by a $1.1 billion increase in expense.

Operational Revenue for the first nine months was $30,807 million, $2,669 million higher than expected.

- Resource revenue was $6,669 million, $1,439 million higher, mainly due to higher oil prices, partly offset by lower natural gas prices and land lease sales.
- Heritage and endowment fund investment income was $843 million greater, due to strong equity markets.
- Personal income tax revenue was up $420 million, from higher 2012 tax year assessments, and population and personal income growth.
- Other notable revenue variances after nine months include: increases of $102 million in the Canada Health Transfer, $57 million in agriculture insurance premiums, $55 million in net liquor income and $51 million in refunds of expense; decreases of $420 million in corporate income tax, due mainly to timing of instalment payments and $58 million in miscellaneous revenue, mainly from lower Fort McMurray land sales.

Operational Expense for the first nine months was $29,567 million, $1,057 million higher than expected, due primarily to increased operating expense and disaster / emergency assistance for flooding.

- Operating expense was $493 million higher than expected, due mainly to increases for health care, post-secondary institutions, school boards and social programs, largely driven by the higher population forecast, and to accelerated policing grants, higher crude oil marketing costs and external investment management fees.
- Disaster / emergency expense was $652 million higher than expected, due primarily to the provision of $537 million for flood assistance and to increased forest fire-fighting costs.

The Contingency Account balance on December 31, 2013 was $2,436 million, and by year end the balance is estimated at about $4.6 billion. The 2013-14 year-end operational results are now expected to be about a $1.4 billion surplus. The nine month results include only a portion of expected flood assistance expense, but no expected disaster recovery federal revenue.

OPERATIONAL PLAN SUMMARY[a]

(millions of dollars)

	2013-14				2012-13	
	Budget	9 Month Estimate	9 Month Actual	Change from Estimate	9 Month Actual	Change
Total Revenue	38,736	28,879	**31,463**	2,584	28,089	3,374
Less:						
Revenue received for capital purposes	(522)	(340)	**(330)**	10	(352)	22
Investment income retained by Heritage Fund	(297)	(223)	**(178)**	45	(165)	(13)
Allocation for Capital Plan debt servicing costs	(238)	(178)	**(148)**	30	(66)	(82)
Operational Revenue	**37,679**	**28,138**	**30,807**	**2,669**	**27,506**	**3,301**
Operational Expense						
Operating expense	36,946	27,458	**27,951**	493	26,473	1,478
Less in-year savings	(400)	-	-	-	-	-
Operating expense (net of in-year savings)	**36,546**	**27,458**	**27,951**	**493**	**26,473**	**1,478**
Disaster / emergency assistance	200	22	**137**	115	587	(450)
2013 Alberta flood assistance	-	-	**537**	537	-	537
Amortization / inventory consumption / loss on disposals	982	730	**672**	(58)	609	63
General debt servicing costs	402	300	**270**	(30)	312	(42)
Total Operational Expense	**38,130**	**28,510**	**29,567**	**1,057**	**27,981**	**1,586**
Operational Surplus / (Deficit)	**(451)**	**(372)**	**1,240**	**1,612**	**(475)**	**1,715**

[a] For fiscal policy purposes under the *Fiscal Management Act*. Does not include revenue or expense of Crown-controlled SUCH sector organizations or Alberta Innovates corporations, or changes in pension liabilities. 2013-14 Budget revenue and operating expense have been increased by $120 million, reflecting changed accounting policy for an allowance for doubtful accounts for corporate income tax, now included in expense instead of being deducted from revenue, and by $4 million reflecting federal revenue and associated expense for French language programs being recognized instead of being treated as a payment based on agreement. 2012-13 nine month Actual revenue and operating expense have been increased by $25 million, reflecting changed accounting policy for crude oil transportation and marketing costs, now included in expense instead of being deducted from crude oil royalty revenue.

REVENUE

(millions of dollars)

	2013-14				2012-13	
	Budget	9 Month Estimate	9 Month Actual	Change from Estimate	9 Month Actual	Change
Income Taxes						
Personal income tax	10,001	7,501	7,921	420	6,944	977
Corporate income tax	4,943	3,618	3,198	(420)	2,962	236
	14,944	**11,119**	**11,119**	**-**	**9,906**	**1,213**
Other Taxes						
Education property tax	1,835	1,376	1,380	4	1,313	67
Tobacco tax	920	690	711	21	697	14
Fuel tax	900	675	683	8	651	32
Insurance taxes	333	250	269	19	237	32
Freehold mineral rights tax	152	114	87	(27)	98	(11)
Tourism levy	85	64	68	4	64	4
	4,225	**3,169**	**3,198**	**29**	**3,060**	**138**
Non-Renewable Resource Revenue						
Bitumen royalty	3,367	2,305	3,922	1,617	3,011	911
Crude oil royalty	1,615	1,245	1,852	607	1,452	400
Natural gas and by-products royalty	965	731	295	(436)	345	(50)
Bonuses and sales of Crown leases	1,148	832	460	(372)	827	(367)
Rentals and fees	145	109	130	21	132	(2)
Coal royalty	10	8	10	2	(6)	16
	7,250	**5,230**	**6,669**	**1,439**	**5,761**	**908**
Transfers from Government of Canada						
Canada Health Transfer	2,597	1,947	2,049	102	1,883	166
Canada Social Transfer	1,374	1,030	1,049	19	982	67
Agriculture support programs	319	292	267	(25)	256	11
Labour market agreements	174	130	142	12	143	(1)
Infrastructure support	370	257	222	(35)	245	(23)
2013 Alberta flood assistance	-	-	-	-	-	-
Other	285	208	208	-	238	(30)
	5,119	**3,864**	**3,937**	**73**	**3,747**	**190**
Investment Income						
Alberta Heritage Savings Trust Fund	1,368	1,026	1,731	705	967	764
Endowment funds	234	175	313	138	182	131
Alberta Capital Finance Authority	279	209	196	(13)	197	(1)
Contingency Account	63	47	60	13	280	(220)
Agriculture Financial Services Corporation	124	93	88	(5)	84	4
Other	77	56	67	11	70	(3)
	2,145	**1,606**	**2,455**	**849**	**1,780**	**675**
Net Income from Government Business Enterprises						
AGLC - Gaming / lottery	1,484	1,113	1,113	-	1,133	(20)
AGLC - Liquor	718	539	594	55	580	14
Alberta Treasury Branches	250	187	215	28	168	47
Other	26	20	22	2	21	1
	2,478	**1,859**	**1,944**	**85**	**1,902**	**42**
Premiums, Fees and Licences						
Motor vehicle licences	485	359	367	8	348	19
Crop, hail and livestock insurance premiums	313	313	370	57	310	60
Energy industry levies	203	203	189	(14)	147	42
Land titles	85	63	67	4	64	3
Land and grazing	69	52	55	3	50	5
Supplementary health benefits premiums	53	40	38	(2)	40	(2)
Other	364	272	254	(18)	193	61
	1,572	**1,302**	**1,340**	**38**	**1,152**	**188**
Other						
AIMCo investment management charges	167	126	164	38	167	(3)
Fines and penalties	126	94	111	17	106	5
Refunds of expense	122	91	142	51	150	(8)
Climate change and emissions management	60	45	68	23	43	25
Miscellaneous	528	374	316	(58)	315	1
	1,003	**730**	**801**	**71**	**781**	**20**
Total Revenue	**38,736**	**28,879**	**31,463**	**2,584**	**28,089**	**3,374**

OPERATING EXPENSE BY MINISTRY[a]

(millions of dollars)

	2013-14				2012-13	
	Budget	9 Month Estimate	9 Month Actual	Change from Estimate	9 Month Actual	Change
Investing in Families and Communities						
Culture	162	121	**120**	(1)	104	16
Health	17,048	12,786	**13,010**	224	11,930	1,080
Human Services	4,155	3,046	**3,172**	126	3,061	111
Justice and Solicitor General	1,253	915	**958**	43	920	38
Municipal Affairs	433	350	**319**	(31)	311	8
Tourism, Parks and Recreation	162	121	**114**	(7)	117	(3)
Securing Alberta's Economic Future						
Education	6,210	4,526	**4,582**	56	4,459	123
Infrastructure	504	365	**369**	4	358	11
Innovation and Advanced Education[b]	2,635	1,981	**2,033**	52	2,008	25
Jobs, Skills, Training and Labour	140	97	**92**	(5)	95	(3)
Service Alberta	243	170	**156**	(14)	162	(6)
Transportation	478	368	**386**	18	354	32
Treasury Board and Finance	1,381	946	**982**	36	966	16
Advancing World-leading Resource Stewardship						
Aboriginal Relations[b]	169	123	**113**	(10)	110	3
Agriculture and Rural Development	845	728	**672**	(56)	739	(67)
Energy	439	298	**428**	130	305	123
Environment and Sustainable Resource Development	478	359	**311**	(48)	332	(21)
International and Intergovernmental Relations	37	28	**23**	(5)	19	4
Other						
Executive Council	51	38	**34**	(4)	34	-
Legislative Assembly	122	92	**77**	(15)	89	(12)
Total Operating Expense	**36,946**	**27,458**	**27,951**	**493**	**26,473**	**1,478**

[a] 2012-13 nine month Actual, and 2013-14 Budget and nine month Estimate numbers, have been restated to reflect the re-organization of government departments in *Budget 2013* and subsequently established by Orders in Council under the *Government Organization Act*, on December 13, 2013 and February 12, 2014.

[b] Numbers have been restated to reflect a transfer of $2 million from Innovation and Advanced Education to Aboriginal Relations.

DISASTER / EMERGENCY ASSISTANCE

(millions of dollars)

	2013-14				2012-13	
	Budget	9 Month Estimate	9 Month Actual	Change from Estimate	9 Month Actual	Change
Agriculture and Rural Development	2	1	**1**	-	272	(271)
Environment and Sustainable Resource Development	-	-	**112**	112	247	(135)
Municipal Affairs	27	21	**24**	3	68	(44)
Unallocated	171	-	**-**	-	-	-
Total	**200**	**22**	**137**	**115**	**587**	**(450)**
2013 Alberta flood assistance:						
Aboriginal Relations	-	-	**1**	1	-	1
Human Services	-	-	**66**	66	-	66
Infrastructure	-	-	**39**	39	-	39
Municipal Affairs	-	-	**431**	431	-	431
Total 2013 Alberta flood assistance	**-**	**-**	**537**	**537**	**-**	**537**
Total Disaster / Emergency Assistance	**200**	**22**	**674**	**652**	**587**	**87**

CAPITAL AMORTIZATION

(millions of dollars)

	2013-14				2012-13	
	Budget	9 Month Estimate	9 Month Actual	Change from Estimate	9 Month Actual	Change
Investing in Families and Communities						
Culture	3	2	**2**	-	2	-
Health	17	13	**12**	(1)	11	1
Human Services	10	8	**7**	(1)	5	2
Justice and Solicitor General	25	19	**16**	(3)	6	10
Municipal Affairs	30	23	**22**	(1)	21	1
Tourism, Parks and Recreation	18	14	**13**	(1)	13	-
Securing Alberta's Economic Future						
Education	3	2	**3**	1	3	-
Infrastructure	102	76	**73**	(3)	64	9
Innovation and Advanced Education	5	4	**4**	-	4	-
Jobs, Skills, Training and Labour	1	-	**1**	1	1	-
Service Alberta	45	34	**30**	(4)	32	(2)
Transportation	435	327	**322**	(5)	302	20
Treasury Board and Finance	22	17	**11**	(6)	6	5
Advancing World-leading Resource Stewardship						
Agriculture and Rural Development	16	12	**12**	-	11	1
Energy	23	17	**15**	(2)	13	2
Environment and Sustainable Resource Development	37	28	**24**	(4)	21	3
Other						
Legislative Assembly	1	1	**2**	1	1	1
Total Amortization Expense	**795**	**597**	**569**	**(28)**	**516**	**53**

INVENTORY CONSUMPTION

(millions of dollars)

	2013-14				2012-13	
	Budget	9 Month Estimate	9 Month Actual	Change from Estimate	9 Month Actual	Change
Investing in Families and Communities						
Culture	1	-	**1**	1	1	-
Health	47	35	**34**	(1)	31	3
Human Services	1	1	**-**	(1)	-	-
Securing Alberta's Economic Future						
Education	11	9	**13**	4	18	(5)
Infrastructure	77	58	**19**	(39)	34	(15)
Service Alberta	9	7	**9**	2	8	1
Transportation	40	22	**22**	-	-	22
Treasury Board and Finance	1	-	**-**	-	-	-
Advancing World-leading Resource Stewardship						
Environment and and Sustainable Resource Development	1	1	**-**	(1)	-	-
Total Inventory Consumption	**187**	**133**	**98**	**(35)**	**92**	**6**

DEBT SERVICING COSTS

(millions of dollars)

	2013-14				2012-13	
	Budget	9 Month Estimate	9 Month Actual	Change from Estimate	9 Month Actual	Change
General						
Agriculture and Rural Development						
Agriculture Financial Services Corporation	75	55	**52**	(3)	50	2
Treasury Board and Finance						
General government	315	236	**209**	(27)	251	(42)
Municipal Affairs						
Alberta Social Housing Corporation	12	9	**9**	-	11	(2)
	402	**300**	**270**	**(30)**	**312**	**(42)**
Capital Plan						
Education						
Alberta Schools Alternative Procurement P3 financing costs	27	19	**20**	1	19	1
Treasury Board and Finance						
Direct borrowing for capital purposes	144	108	**80**	(28)	-	80
Transportation						
Ring road P3 financing costs	67	51	**48**	(3)	47	1
	238	**178**	**148**	**(30)**	**66**	**82**
Total Debt Servicing Costs	**640**	**478**	**418**	**(60)**	**378**	**40**

2013–14 FINANCING REQUIREMENTS

(millions of dollars)

	2013-14				2012-13	
	Budget	9 Month Estimate	9 Month Actual	Change from Estimate	9 Month Actual	Change
Financing Requirements / Completed to Date						
Direct borrowing for capital purposes	3,190	2,393	**2,723**	330	-	2,723
Term debt borrowing for provincial corporations:						
Agriculture Financial Services Corporation	365	274	**120**	(154)	225	(105)
Alberta Capital Finance Authority	3,385	2,539	**3,488**	949	2,912	576
Alberta Treasury Branches	400	300	**500**	200	1,000	(500)
Total Financing Requirements / Completed to Date	**7,340**	**5,506**	**6,831**	**1,326**	**4,137**	**2,694**

[a] Does not include $750 million borrowed since December 31, 2013 ($500 million for capital purposes; $250 million for ACFA).

INVENTORY ACQUISITION

(millions of dollars)

	2013-14				2012-13	
	Budget	9 Month Estimate	9 Month Actual	Change from Estimate	9 Month Actual	Change
Investing in Families and Communities						
Culture	1	-	-	-	1	(1)
Health	47	35	**29**	(6)	29	-
Human Services	1	1	-	(1)	1	(1)
Securing Alberta's Economic Future						
Education	12	9	**12**	3	15	(3)
Infrastructure	52	39	**13**	(26)	37	(24)
Service Alberta	9	7	**9**	2	8	1
Transportation	40	25	**27**	2	28	(1)
Advancing World-leading Resource Stewardship						
Environment and Sustainable Resource Development	1	1	-	(1)	-	-
Total Inventory Acquisition	**163**	**117**	**90**	**(27)**	**119**	**(29)**

Capital Plan Highlights

Capital Plan actual results for the first nine months of 2013-14 were essentially on track with the overall estimate in *Budget 2013*.

- Actual nine month Capital Plan spending was $3,506 million, $59 million higher than expected. While there are variances in most areas, these mainly reflect changes related to project progress. No projects have been cancelled.
- The $224 million increase in Transportation is mainly from the carry-over of 2012-13 projects and costs related to the Southwest Calgary ring road project. The remainder of the changes reflect re-profiling of project cash flows within the current year and from 2012-13, some of which will likely adjust over the remainder of 2013-14.
- Revenue for capital purposes was $10 million lower than estimated, mainly from fewer-than-anticipated completed applications from municipalities under the Federal Gas Tax Fund and to delayed Canada ecoTrust spending.
- Direct borrowing for the Capital Plan was $330 million higher than expected, due mainly to increased financing needs for projects re-profiled from 2012-13 and to market opportunities. The withdrawal from the Capital Plan financing account was consequently $260 million lower.

CAPITAL PLAN SUMMARY

(millions of dollars)

	2013-14				2012-13	
Summary	Budget	9 Month Estimate	9 Month Actual	Change from Estimate	9 Month Actual	Change
Capital Plan Spending	**5,209**	**3,447**	**3,506**	**59**	**3,286**	**220**
Capital Plan Financing						
Revenue received for capital purposes	522	340	**330**	(10)	352	(22)
Retained income of funds and agencies for capital purposes	84	63	**56**	(7)	5	51
Disposal of capital assets	2	-	-	-	-	-
Alternative financing (P3s)	344	258	**264**	6	198	66
Direct borrowing	3,190	2,393	**2,723**	330	-	2,723
Withdrawal from Capital Plan financing account	1,067	393	**133**	(260)	-	133
Transfer from Contingency Account	-	-	-	-	2,731	(2,731)
Total Capital Plan Financing	**5,209**	**3,447**	**3,506**	**59**	**3,286**	**220**
By Ministry						
Investing in Families and Communities						
Culture	54	40	**21**	(19)	18	3
Health	104	56	**22**	(34)	36	(14)
Human Services	9	7	**5**	(2)	6	(1)
Infrastructure (health facilities)	576	288	**235**	(53)	249	(14)
Justice and Solicitor General	87	66	**25**	(41)	69	(44)
Municipal Affairs	921	900	**865**	(35)	859	6
Tourism, Parks and Recreation	19	14	**12**	(2)	9	3
Transportation (municipal support)	751	305	**327**	22	325	2
Securing Alberta's Economic Future						
Education	564	361	**372**	11	226	146
Infrastructure	214	137	**150**	13	133	17
Innovation and Advanced Education	68	53	**65**	12	65	-
Jobs, Skills, Training and Labour	1	1	**1**	-	1	-
Service Alberta	41	22	**18**	(4)	10	8
Transportation	1,409	880	**1,082**	202	1,099	(17)
Treasury Board and Finance	29	22	**31**	9	30	1
Advancing World-leading Resource Stewardship						
Agriculture and Rural Development	34	30	**31**	1	30	1
Energy	197	167	**108**	(59)	46	62
Environment and Sustainable Resource Development	126	94	**92**	(2)	75	17
Other						
Legislative Assembly	5	4	**11**	7	-	11
2013 Alberta flood assistance						
Education	-	-	**9**	9	-	9
Environment and Sustainable Resource Development	-	-	**23**	23	-	23
Infrastructure	-	-	**1**	1	-	1
Total Capital Plan	**5,209**	**3,447**	**3,506**	**59**	**3,286**	**220**

ECONOMIC OUTLOOK

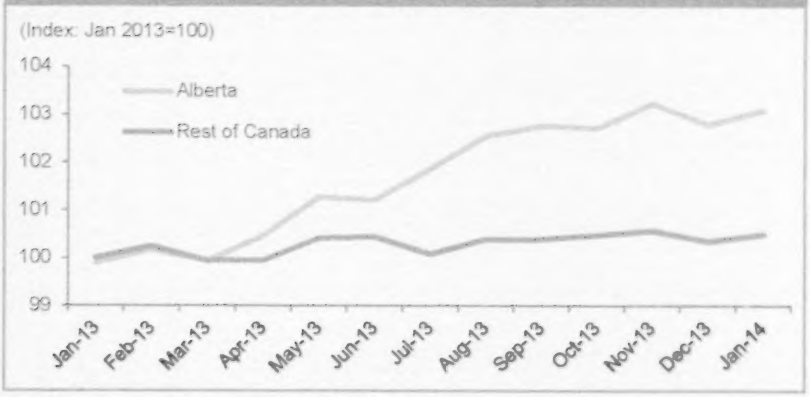
Alberta's economy enters 2014 firing on all cylinders

The Alberta economy gained momentum through 2013 and is off to a strong start this year. Growth is widespread, with many indicators gathering strength in the second half of last year.

In the household sector, the province saw solid job growth throughout 2013 even as the national job market slowed. New housing activity strengthened in 2013, and into this year, as migrants continued to enter the market. Record net migration in 2013 has not only helped fuel consumption and housing, it has also provided Alberta with a source of labour during its expansion. In the business sector, output has also accelerated following a weak start to 2013.

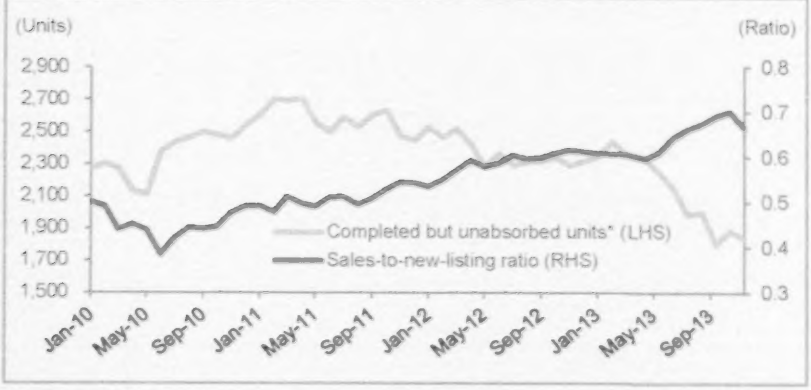
Overall, the Alberta economy grew by an estimated 3.3% in 2013. This is slightly higher than the expected 2.9% increase at *Budget 2013*, reflecting flood reconstruction activity and stronger-than-forecast population growth. In 2014, real GDP growth is expected to accelerate to 3.7%, lifted by exports, residential and business investment, as well as flood-related spending.

Figure 1. Employment Growth



Sources: Statistics Canada

Figure 2. Alberta Resale and New Housing Indicators



Sources: CMHC and CREA
* Edmonton and Calgary only.
Sales-listing ratio above 0.6 denotes a seller's market.

Alberta Household Sector

Labour market spurs migration

Alberta households were a major driver of economic activity in 2013. Retail sales rose by an estimated 6.7% for the second straight year, led by motor vehicle sales.

Alberta's robust labour market continues to underpin gains in the household sector. Strong job growth persisted through most of 2013 and into 2014, even as gains in the rest of Canada slowed to a crawl (Figure 1). Alberta added an average of 5,700 jobs per month in 2013 compared with only 2,600 in all other provinces. Alberta holds more than a fifth of all job vacancies in Canada, pointing to further job growth ahead. With momentum heading into 2014, strong employment growth of 2.6% is expected this year. Not surprisingly, the labour market has attracted record inflows of migrants. Alberta's population surged past four million in 2013, growing by the highest rate since 1981 at 3.5%. In 2014, population growth is forecast to moderate, but remain solid at 2.9%.

Housing market tightens

Alberta's housing market has been buoyed by a persistent influx of migrants. The resale market is now firmly in sellers' territory, while the number of completed but unabsorbed units in Calgary and Edmonton has fallen close to a 6-year low (Figure 2). The tightening of the market has pushed rents higher, and led to some modest pressure on housing prices. The ongoing transition of new migrants

ECONOMIC OUTLOOK

from rental to owned accommodation is expected to support further gains in housing activity in the province. Housing starts are forecast to increase to 38,300 in 2014.

Strong but steady wage growth

In-migration has lifted labour supply and kept wage growth contained. Recent growth in average weekly earnings has been around 3.5%, below the ten-year average. Based on a stronger outlook for employment and population, the forecast for 2014 household income growth has been upgraded since *Budget 2013*.

Consumer prices rose at an average rate of 1.4% in 2013, the second straight year below 2% and well below growth in wages. Strong in-migration, coupled with slack in the global economy, has contributed to low price inflation and allowed Alberta to grow quickly without triggering major inflation pressures. Inflation is expected to pick-up slightly in 2014 to 2.2%, due to stronger shelter costs and a weaker Canadian dollar.

Alberta Business Sector

Output accelerates through 2013

Exports jumped in the second half after being slowed by maintenance outages at refineries and delays at oil sands facilities earlier in the year (Figure 3). The rebound in production coincided with higher prices for oil produced in Alberta relative to the previous year. Manufactured product sales also reversed a weak start in 2013. In the agriculture sector, farmers witnessed a bumper crop in 2013, as favourable weather conditions pushed wheat and canola production to record heights.

Crude by rail surges

Moving crude oil products by rail took off in 2013 amid ongoing constraints in the pipeline network. With new onloading facilities being developed, further increases in crude shipments by rail are expected.

Building activity trends higher

Alberta's fast growing economy and population, along with flood recovery efforts, supported the construction sector in 2013. Non-residential building construction investment rose 3.4%, due to gains in the industrial and institutional/government sectors. Building permits continue to trend higher, pointing to further construction gains ahead. Despite strong activity, construction cost increases have remained below historic norms in Calgary and Edmonton.

Dollar hits 4 ½ year low

The Canadian dollar has dropped sharply against the US dollar, averaging 90 US¢/C$ in recent weeks (see page 13-14). Based on recent developments, the exchange rate forecast for 2013-14 has been lowered to 95.1 US¢/C$.

Oil price outlook largely unchanged

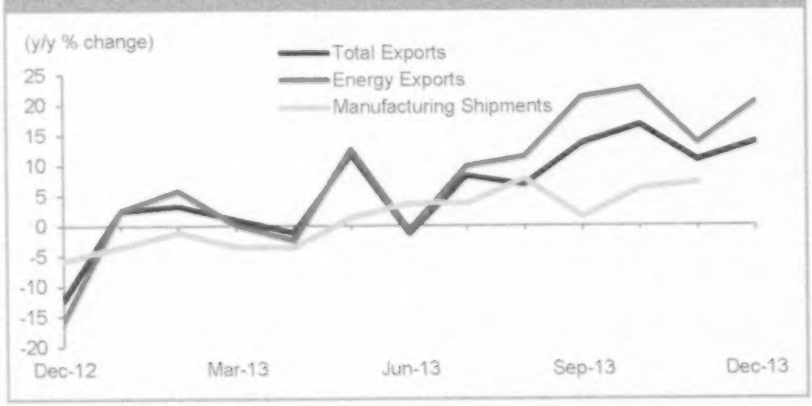
The oil price outlook for 2013-14 remains up from *Budget 2013*, but roughly in line with *Second Quarter*. Oil price differentials remain highly volatile due to lack of spare capacity in the pipeline network. Natural gas prices have risen in recent months due to abnormally cold weather in North America. However, due to weaker prices through most of 2013, the ARP forecast for 2013-14 is roughly unchanged from *Budget 2013*.

External Risks

Global economic growth is picking up, led by improvements in advanced economies. However, as a commodity and trade driven economy, Alberta is subject to a number of risks:

- With a shortage of pipeline capacity, the price of Alberta oil is volatile and highly susceptible to transportation and refinery disruptions.
- Unwinding the Federal Reserve's unprecedented quantitative easing program could cause further volatility in financial markets and weigh on emerging market economies. A further slowdown in emerging markets would hurt global demand and commodity prices.
- The US economy is gaining momentum, and remains an upside risk to the forecast.
- Faster-than-expected global growth could put upward pressure on oil prices, boosting Alberta investment and employment.

Figure 3. Alberta Exports and Manufacturing Shipments



Sources: Statistics Canada

KEY ENERGY AND ECONOMIC ASSUMPTIONS

Fiscal Year Assumptions	2013–14 9 Month Actual	2013–14 Fiscal Year Forecast			
		Budget	1st Quarter	2nd Quarter	3rd Quarter
Prices					
Crude Oil Price					
WTI (US$/bbl)	99.17	92.5	94.81	98.96	98.16
Alberta Wellhead (Cdn$/bbl)[a]	90.00	82.99	84.3	91.52	89.42
WCS @ Hardisty (Cdn$/bbl)	79.01	68.21	74.51	80.38	78.54
Natural Gas Price					
Alberta Reference Price (Cdn$/GJ)	2.85	3.07	3.14	2.97	3.09
Production					
Conventional crude oil (000s barrels/day)	580	550	592	588	583
Raw bitumen (000s barrels/day)	1,979	2,140	2,160	2,138	2,065
Natural gas (billions of cubic feet)	3,139	3,873	3,882	3,938	4,004
Interest rates					
3-month Canada treasury bills (per cent)	0.97	1.05	1.05	1.00	0.95
10-year Canada bonds (per cent)	2.38	2.3	2.65	2.55	2.50
Exchange Rate (US¢/Cdn$)	96.4	99.0	98.0	97.5	95.1

Calendar Year Assumptions	2013 Estimates	2014 Forecast		
		Budget	2nd Quarter	3rd Quarter
Gross Domestic Product				
Nominal (millions of dollars)	331,927	339,028	348,452	352,143
per cent change	6.4	5.4	5.0	6.1
Real (millions of 2007 dollars)	298,038	301,720	308,831	308,980
per cent change	3.3	2.9	3.5	3.7
Other Indicators				
Employment (thousands)	2,211	2,227	2,257	2,268
per cent change	2.9	1.7	2.4	2.6
Unemployment rate (per cent)	4.6	4.3	4.4	4.4
Average Weekly Earnings (per cent change)	3.2	3.3	3.5	3.4
Primary Household Income (per cent change)	7.1	5.2	5.9	6.7
Net Corporate Operating Surplus (per cent change)	9.4	10.3	4.3	8.4
Housing starts (number of units)	36,000	31,900	35,300	38,300
Alberta Consumer Price Index (per cent change)	1.4	1.8	2.0	2.2
Population (July 1st, thousands)	4,025	4,054	4,128	4,140
per cent change	3.5	2.0	2.6	2.9

[a] Refers to the average price per barrel of Alberta light, medium and heavy oil.

THE CANADIAN DOLLAR

What does a weaker loonie mean for Alberta?

One of the most noteworthy financial developments in recent months has been the decline of the Canadian dollar. While the dollar has been trending downward for well over a year, the depreciation has accelerated since early 2014. The loonie hit a 4.5 year low against the US dollar in late January at 89 US¢/Cdn$ and has been trading around 90 US¢/Cdn$ in recent weeks (Figure 1). The contributing factors to this decline and the impact of a lower loonie on Alberta are discussed below.

Canadian dollar loses some of its appeal

In the years following the recession, Canada was an appealing investment destination given its historically stable financial system and relatively low federal debt levels. These factors kept demand for Canadian securities high and the loonie elevated near parity despite weak export performance and large trade deficits. Another factor was the prospect of higher returns, as the Bank of Canada suggested it may raise interest rates to help curb rising levels of household debt.

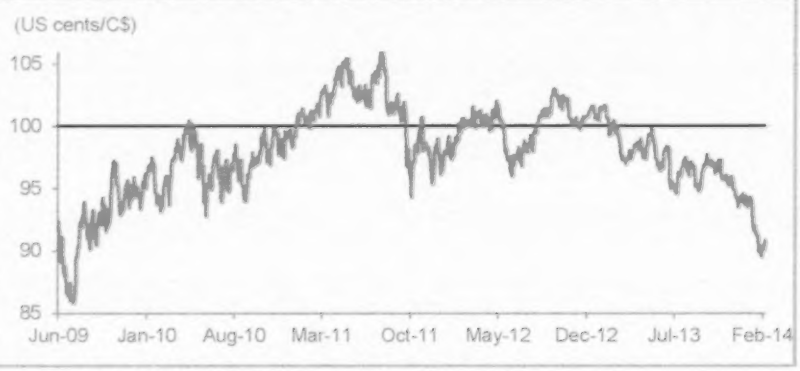
Over the course of 2013 many of the factors that were lending strength to the dollar receded. Risk globally was reduced as Europe made tentative steps towards recovery and US lawmakers compromised on a budget, reducing fiscal uncertainty. While this is undoubtedly positive for the global economy, it also gives foreign investors less incentive to seek the safety of Canadian assets at a time when they were already becoming more risk tolerant. These factors have contributed to a drop off in net portfolio inflows into Canada (Figure 2).

Financial inflows have also suffered from lower expected returns as the Bank of Canada has communicated to markets that it expects interest rates to remain low for longer than it previously anticipated. This reflects a shift in concern away from household debt and towards below target inflation. As a result of weak demand, inflation in Canada has been persistently low and repeatedly come in below the Bank's forecast. The Bank has emphasized that a lower Canadian dollar could improve Canada's export performance, suggesting that it is comfortable with a lower exchange rate.

Two sides to the story

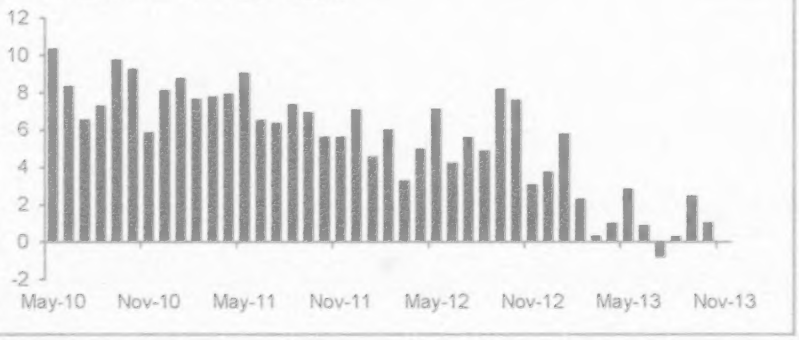
Canada is only one side of the story. A stronger US dollar has also contributed to some of the depreciation. The outlook for the US economy has improved, lending strength to the US dollar. A brighter outlook also allows the Federal Reserve to pare back stimulus, which adds further support by increasing US interest rates. Due to US dollar strength, the loonie has fallen further against the US dollar than it has against the next ten most traded currencies on average (Figure 3).

Figure 1. US - Canada Exchange Rate



Source: Bank of Canada. Last observation is February 7, 2014

Figure 2. Net Purchases of Canadian Securities*



Source: Statistics Canada

* Foreign purchases of Canadian securities less domestic purchases of foreign securities

THE CANADIAN DOLLAR

Based on this basket of currencies, slightly more than a quarter of the depreciation since the start of 2013 has been due to US dollar strengthening.

The impact on Alberta's economy

A depreciation of the Canadian dollar benefits Alberta primarily through exports. Exporters with prices denominated in US dollars receive a higher Canadian dollar price after a depreciation, which leads to higher revenues. Exporters with prices denominated in Canadian dollars become more competitive following a depreciation as their goods become less expensive for their US customers. Albertans who hold US assets will benefit as the Canadian dollar value of these assets increases following a depreciation.

On the other hand, import prices increase with a lower dollar, which increases costs for consumers and businesses. Many consumer goods are imported so higher import prices eventually result in higher prices for consumers, though research suggests this adjustment occurs gradually over several years. Businesses will also face higher costs as imported parts and materials become more expensive as does investing in machinery and equipment.

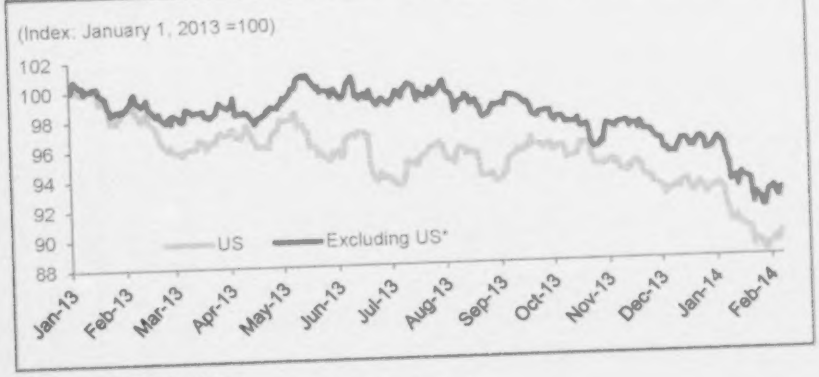
A boost to royalties

The Government of Alberta's royalty revenue is sensitive to changes in the exchange rate. Energy prices are determined in the global market and mainly priced in US dollars. When the Canadian dollar depreciates, producers earn more Canadian dollar revenue on the same energy prices. This increases the revenue base from which the province collects royalties.

Royalties can also increase due to changes in the royalty rate itself. The royalty rate that oil sands projects pay under the generic royalty regime is directly linked to the WTI price in Canadian dollars (Figure 4). All else being equal, a lower dollar increases the Canadian dollar price of oil, thereby increasing the royalty rate paid by oil sands producers. The higher producer revenue can also push oil sands projects into their "payout" period sooner, meaning producers have received enough revenue to cover their capital costs on a particular project. This is important as producers in the payout period are subject to a higher royalty rate on net revenue, which boosts future royalty revenues.

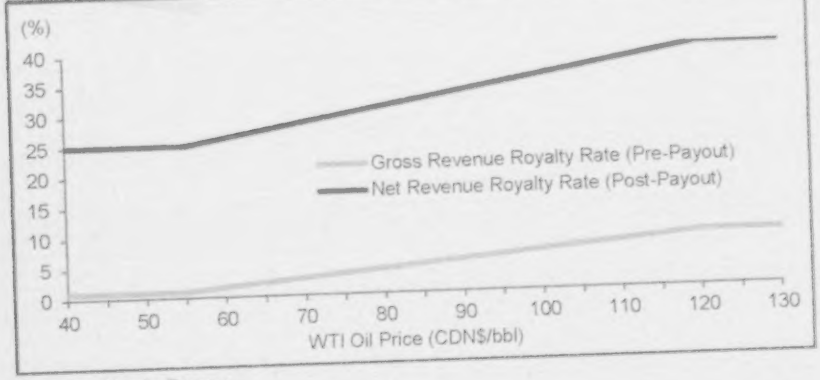
An offsetting factor is that a lower loonie can raise many direct costs that are deductible for royalty purposes. Imported equipment, for example, will cost more as the Canadian dollar depreciates. The net impact of a lower Canadian dollar is positive in terms of provincial royalty revenue. For small movements in the Canadian dollar, the estimated impact of a 1 US¢ decline is about $160 million in additional government revenue in 2013-14.

Figure 3. Canadian Dollar Against Different Currencies



Sources: Haver Analytics,
* Basket of 10 most traded non-US currencies.

Figure 4. Alberta Royalty Rates for Oil Sands Projects



Source: Alberta Energy

REVENUE IMPACTS

Impact of recent developments on government revenue

The revenue outlook for 2013-14 has been revised higher from *Budget 2013*, and is up slightly from *Second Quarter*. The upgrade from *Budget 2013* reflects higher-than-expected energy prices, a stronger forecast for income tax revenues, and a weaker Canadian dollar.

Royalty revenue forecast edges higher

Relative to *Budget 2013*, the main factors that have raised the royalty revenue forecast for 2013-14 are:

- A higher forecast for crude oil prices in North America (i.e., West Texas Intermediate) of US$98.16/bbl (Figure 1). The world oil price (e.g. Brent) has been supported by stronger global demand and supply concerns in the Middle East. After narrowing sharply in the summer, the differential between WTI and the Brent price has widened again, reflecting a softening of US refinery demand and record levels of US crude production.
- The differential between WTI and the price Alberta oil sands producers receive for bitumen (i.e., Western Canada Select) is now forecast at 24%, narrower than the *Budget 2013* forecast of 27%. This differential remains volatile, in large part due to limited pipeline capacity leaving Alberta.
- The recent depreciation of the Canadian dollar has led to a downward revision to the exchange rate forecast to 95.1 US¢/Cdn$ for the fiscal year, down from *Budget 2013* (99.0) and *Second Quarter* (97.0). A lower Canadian dollar boosts royalty revenue (see pg. 14).

Despite a recent jump in production, natural gas royalties are expected to come in slightly below the *Budget 2013* forecast in 2013-14, reflecting higher processing costs and higher deductions related to deeper gas wells.

Alberta land sales are expected to be lower than *Budget 2013* in 2013–14 due to a lower price received per hectare and a lower number of hectares sold.

Income tax forecast improves

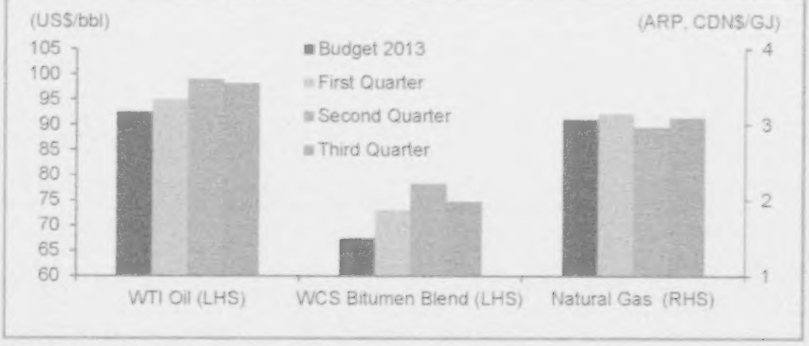
Alberta remains in a robust economic expansion. Higher-than-expected employment growth in 2013, combined with healthy wage gains, have supported large gains in labour income. Strong population growth has also contributed to higher household incomes, driving transfer payments and property income higher. As a result, personal income tax revenue is expected to post another solid increase this fiscal year. Overall, the forecast for personal income tax revenue has been revised higher from *Budget 2013* and *Second Quarter* due to an upgrade in the primary household income forecast as well as strong 2012 tax assessment data.

The business sector is benefiting from Alberta's strong economic growth and energy prices, pushing corporate profits higher. However, flood-related costs, strong wage growth and rising transportation costs have limited overall growth in corporate profits in 2014, as measured by net corporate operating surplus. Overall, the forecast for 2013-14 corporate income tax revenue has increased slightly from *Budget 2013*.

Risks to the revenue outlook

Going forward, the Government of Alberta's revenue is subject to a number of external risks. On the downside, a slowdown in emerging market growth could cause energy prices to stumble. Pipeline project delays or a faster-than-anticipated increase in US oil production would also put downward pressure on the WTI price. On the upside, the US economy is gaining momentum, which could lead to stronger-than-expected global growth and higher commodity prices.

FIGURE 1. Key Energy Price Assumptions for 2013–14



Source: Alberta Energy.
ARP is the Alberta Reference Price for natural gas